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PROJECT NO. 38533

PUC REVIEW OF ERCOT BUDGET

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PUBLIC UTILITY COMMISSION

OF TEXAS

**TEXAS INDUSTRIAL ENERGY CONSUMERS' COMMENTS ON ERCOT'S 2024/2025
BIENNIAL BUDGET AND SYSTEM ADMINISTRATION FEE SUBMISSION**

I. INTRODUCTION

Texas Industrial Energy Consumers (TIEC) appreciates the opportunity to provide public comment at the workshop held in this Project on October 13, 2023. Given the limited scope of public comment, TIEC has prepared these written comments to provide the Commission with additional detail regarding its concerns with ERCOT's biennial budget and System Administration Fee submission.

ERCOT plays a critical role in providing reliable power to Texans, and the Commission should ensure that it is appropriately funded. This is particularly true for ERCOT's core reliability functions and the associated personnel and resources. However, at a time when electricity costs in ERCOT have risen substantially due to market design changes and, more recently, record-breaking heat, the Commission should be very careful and conservative in approving charges that will increase retail customers' electricity bills without adequate support.

TIEC has identified three primary concerns with ERCOT's proposed budget and System Administration Fee request. First, ERCOT appears to have used unreasonable assumptions in projecting the amount of interest income it will earn in coming years. These assumptions also appear to contradict ERCOT's internal financial statements. As detailed below, using more realistic assumptions would significantly reduce or potentially eliminate the need for ERCOT's requested System Administration Fee increase. Second, if a System Administration Fee increase is still necessary in light of this correction, the Commission should seriously consider an approach similar to ERCOT's "Option 2," which would involve a smaller fee increase now with the possibility of an additional adjustment in ERCOT's next budget review. TIEC has heard ERCOT's perspective that a larger fee now will require fewer adjustments in the future; however, as a trade association representing the largest customers that will pay this fee, TIEC would prefer that the

Commission set a reasonable fee now even if that might require adjustments in the coming years. And finally, the Commission should require ERCOT to provide additional information before approving the increase in certain employee positions and department budgets surrounding ERCOT's legal and government/regulatory functions related to ERCOT's "Strategic Objective 3." Without further justification, TIEC is concerned that some of these budgeted items may not be in the interests of the consumers that will be funding them. These issues are addressed in detail below.

II. ISSUES WITH ERCOT'S BUDGET SUBMISSION

A. ERCOT did not justify its projected drop in interest income, which is a significant driver of the System Administration Fee increase.

First, ERCOT's projected drop in interest from the Congestion Revenue Rights (CRR) Fund Balance (CRR Fund) appears to be unreasonable in light of historical data. ERCOT has assumed that the interest it earns on the CRR Fund will drop from \$104.7 M in 2023¹ to \$49.8 M in 2024 and \$39.8 M in 2025.² ERCOT proposes to increase the System Administration Fee, which is ultimately paid by electric consumers, to make up the resulting budget shortfall.

Two assumptions dictate ERCOT's projected interest income: (1) the anticipated size of the CRR Fund, and (2) the anticipated interest rate. ERCOT included a sensitivity analysis in its budget submission that shows the System Administration Fee increase needed at different assumed CRR Funds and interest rates. These assumptions have a massive impact on the appropriate System Administration Fee increase. This is illustrated in the chart below, which shows the incremental increase (positive) or decrease (negative) to ERCOT's proposed System Administration Fee that would be required under different CRR Fund balance and interest rate assumptions:

¹ In ERCOT's original Budget Submission, it anticipated interest income of \$77.4 million in 2023. *See* ERCOT Budget Submission at 18, line 11. On October 20, 2023, ERCOT filed a Supplemental Budget Submission indicating that its most recent interest income projections had risen by \$27.3 million since the time it prepared its Budget Submission. *See* Supplemental Information Regarding ERCOT's 2024/2025 Biennial Budget and System Administration Fee Submission ("Supplemental Budget Submission") at 7, line 3 (Oct. 20, 2023).

² *See* ERCOT Budget Submission at 18, line 11.

Figure 1: ERCOT's Sensitivity Analysis on Interest Income Assumptions³

\$ in Millions, except rates															
Average Annual Interest Income Rate (2024-2027)	Average Annual CRR Funding Balance (2024-2027)														
	\$	1,250.0	\$	1,500.0	\$	1,750.0	\$	2,000.0	\$	2,250.0	\$	2,500.0	\$	2,750.0	
	0.50%	\$	0.074	\$	0.072	\$	0.069	\$	0.067	\$	0.064	\$	0.062	\$	0.059
	1.00%	\$	0.062	\$	0.056	\$	0.051	\$	0.046	\$	0.041	\$	0.036	\$	0.031
	1.50%	\$	0.049	\$	0.041	\$	0.033	\$	0.026	\$	0.018	\$	0.010	\$	0.003
	2.13%	\$	0.033	\$	0.022	\$	0.011	\$	-	\$	(0.011)	\$	(0.022)	\$	(0.033)
	2.50%	\$	0.023	\$	0.010	\$	(0.003)	\$	(0.015)	\$	(0.028)	\$	(0.041)	\$	(0.054)
	3.00%	\$	0.010	\$	(0.005)	\$	(0.021)	\$	(0.036)	\$	(0.051)	\$	(0.067)	\$	(0.082)
	3.50%	\$	(0.003)	\$	(0.021)	\$	(0.039)	\$	(0.056)	\$	(0.074)	\$	(0.092)	\$	(0.110)

Given that ERCOT's projected interest income has such a significant impact on the System Administration Fee, the Commission should carefully vet ERCOT's underlying assumptions. As explained below, ERCOT's assumptions for both the interest rate and the CRR Fund balance appear to be unrealistically low or, at best, are poorly supported. This drives ERCOT's request to substantially increase the System Administration Fee at customers' expense. It is critical to note that, as discussed below, interest rates today are projected to be over 5% for 2024-2025. Because ERCOT assumes it will earn 1% below market interest rates (which is another questionable assumption), a projected 5% interest rate would translate to 4% on the sensitivity chart above—outside the bounds of the table.

1. ERCOT's assumed interest rate is based on stale Federal Funds rate projections that, when updated, significantly reduce the appropriate System Administration Fee increase.

ERCOT's projected interest earnings are based on a stale forecast of the Federal Funds rate that should be updated. As the Commission is undoubtedly aware, market interest rates have

³ *Id.* at 54.

moved up significantly since ERCOT prepared its Budget Submission. This is further evidenced by ERCOT's Supplemental Budget Submission, which acknowledged that ERCOT's anticipated interest income for 2023 is now **\$27.3 million higher** than it was when ERCOT prepared its original Budget Submission.⁴ Below is the Federal Funds rate projection that ERCOT used in its Budget Submission:

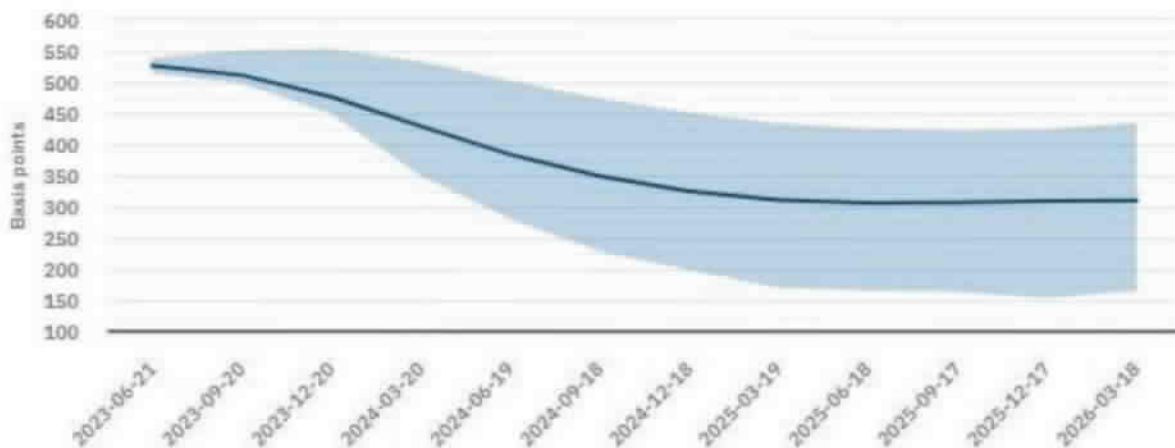
Figure 2: Federal Reserve Projections Used in ERCOT's Budget Submission⁵

The Expected Future Path of the Three-Month Average Fed Funds Rate

Current target range: 500 - 525 basis points

Source: Atlanta Fed (as of 5/23/23)

<https://www.atlantafed.org/cenfig/market-probability-tracker>



As ERCOT's presentation notes, the Federal Reserve projections underlying ERCOT's interest rate assumptions were pulled *five months ago* on May 23, 2023.⁶ The Federal Reserve's projections have changed significantly since then. Below is an updated chart from the same source as of October 23, 2023:

⁴ Supplemental Budget Submission at 1.

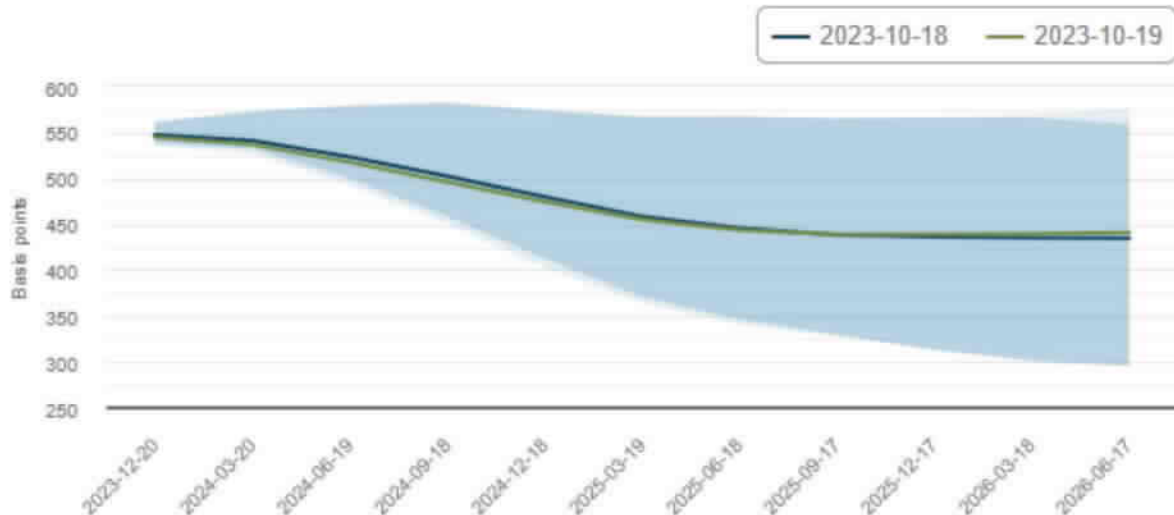
⁵ Budget Submission at 54.

⁶ *Id.* at 55.

Figure 3: Current Federal Reserve Rate Projections⁷

The Expected Three-Month Average SOFR Path

Current target range: 525 - 550 basis points



Critically, this updated chart⁸ shows that anticipated rates are now *significantly higher* than when ERCOT assembled its budget request. Note that *lowest* projected rate for the 2025/2026 period in the updated chart is approximately 450 basis points (4.5%), while ERCOT's outdated projections have a low end of 300 basis points (3.0%). Updating this interest rate assumption has a dramatic impact on the appropriate System Administration Fee increase. As ERCOT explained in its budget submission, "*Every 1% change in the average interest rate from 2024-2027 is approximately equal to a \$0.04 change in the System Administration Fee.*"⁹ Accordingly, simply updating ERCOT's Federal Funds rate projections lowers the projected System Administration Fee increase by \$0.06/MWh.

Further, if the Commission rejects ERCOT's assumption that it will earn 1% below a market rate on its investments (which it should reject, as discussed below) and instead assumes

⁷ Pulled from <https://www.atlantafed.org/cenfig/market-probability-tracker> on October 23, 2023.

⁸ SOFR is "Secured Overnight Financing Rates," which are broad average interest rates for borrowing against Treasury securities." This is the same source used for the prior ERCOT interest rate inputs.

⁹ ERCOT Budget Submission at 54 (emphasis added).

that ERCOT will earn roughly the Federal Funds rate (as it is today), then that would lower the projected System Administration Fee increase that ERCOT needs by *\$0.10/MWh*.

2. There is no basis for ERCOT's assumption that it will earn interest at a rate that is 1% lower than the projected Federal Funds Rate.

ERCOT has not justified its assumption that it will earn interest at a rate that is a full percentage point (100 basis points) below the Federal Reserve's projections.¹⁰ ERCOT claims that its forecasted interest rate for 2023 is 3.72%, and projects the rate will fall to 2.5% in 2024 and 2.0% in 2025.¹¹ These rates are well below what ERCOT is currently earning on its investments and contrary to recent trends in ERCOT's investment yields.

In a presentation to ERCOT's Finance and Audit Committee on October 16, 2023, ERCOT's Chief Financial Officer stated that "*ERCOT's investment yields continue to increase*. As of the end of August 2023, ERCOT's Money Market Mutual Fund (MMMF) yields equaled approximately *5.21%* and the purchase yield of ERCOT's U.S. Treasury Obligation Portfolio equaled approximately *4.82%*."¹² Further, the same report indicated that on September 27, 2023, ERCOT invested \$1.335 billion of funds it holds into short-term U.S. Treasury Bonds to "allow for less interest rate volatility."¹³ As shown in the chart below, those bonds are all expected to mature between now and the end of 2025, and will earn a projected yield of *5.41%*.

¹⁰ *Id.* at 56.

¹¹ *Id.* at 18, Line 11A.

¹² ERCOT Finance and Audit Committee Meeting, Item 5.2: Periodic Report on Investments at 2 (Oct. 16, 2023) (available at: <https://www.ercot.com/files/docs/2023/10/06/5.2%20Periodic%20Report%20on%20Investments.pdf>) (emphases added).

¹³ *Id.* at 6.

Figure 4: Chart Summarizing ERCOT's Current Treasury Portfolio¹⁴

U.S. Treasury Obligation Portfolio Investments Purchased September 27, 2023

Maturity	Par Value	Coupon Rate	Yield
12/15/2023	\$ 31,000,000	0.125%	5.35%
1/25/2024	51,000,000	0.000%	5.39%
2/22/2024	53,000,000	0.000%	5.42%
3/31/2024	108,000,000	2.125%	5.43%
4/30/2024	99,000,000	2.250%	5.50%
5/31/2024	75,000,000	2.000%	5.53%
6/30/2024	76,000,000	1.750%	5.52%
8/31/2024	83,000,000	1.250%	5.54%
9/30/2024	81,000,000	1.500%	5.51%
10/15/2024	80,000,000	0.625%	5.49%
11/30/2024	58,000,000	1.500%	5.44%
12/15/2024	53,000,000	1.000%	5.44%
1/31/2025	64,000,000	1.375%	5.42%
2/15/2025	67,000,000	2.000%	5.41%
3/31/2025	70,000,000	2.625%	5.35%
4/30/2025	66,000,000	2.875%	5.33%
5/15/2025	37,000,000	2.125%	5.30%
6/30/2025	37,000,000	2.750%	5.25%
7/31/2025	34,000,000	0.250%	5.21%
8/15/2025	39,000,000	2.000%	5.21%
9/30/2025	37,000,000	3.000%	5.15%
10/31/2025	36,000,000	0.250%	5.12%
Total	\$ 1,335,000,000		5.41%

Key Takeaway: Bond Portfolio will allow for less interest rate volatility while matching maturities with projected cash flow and liquidity requirements

Notably, 5.41% of this \$1.335 billion investment is approximately \$72.22 million, which is nearly as much as the \$84.4 million in *total* interest income that ERCOT's Budget Submission assumes for 2024/2025.¹⁵ Yet, this investment is only a fraction of ERCOT's total portfolio, as it also has \$4.472 billion in money market funds that yield 5.21%, for projected "*Monthly Investment Income*" of \$17.751 million.¹⁶

¹⁴ *Id.*

¹⁵ ERCOT Budget Submission at 18, Line 11A (\$49.8 M in 2024 + \$34.6 M in 2025 = \$84.4 M).

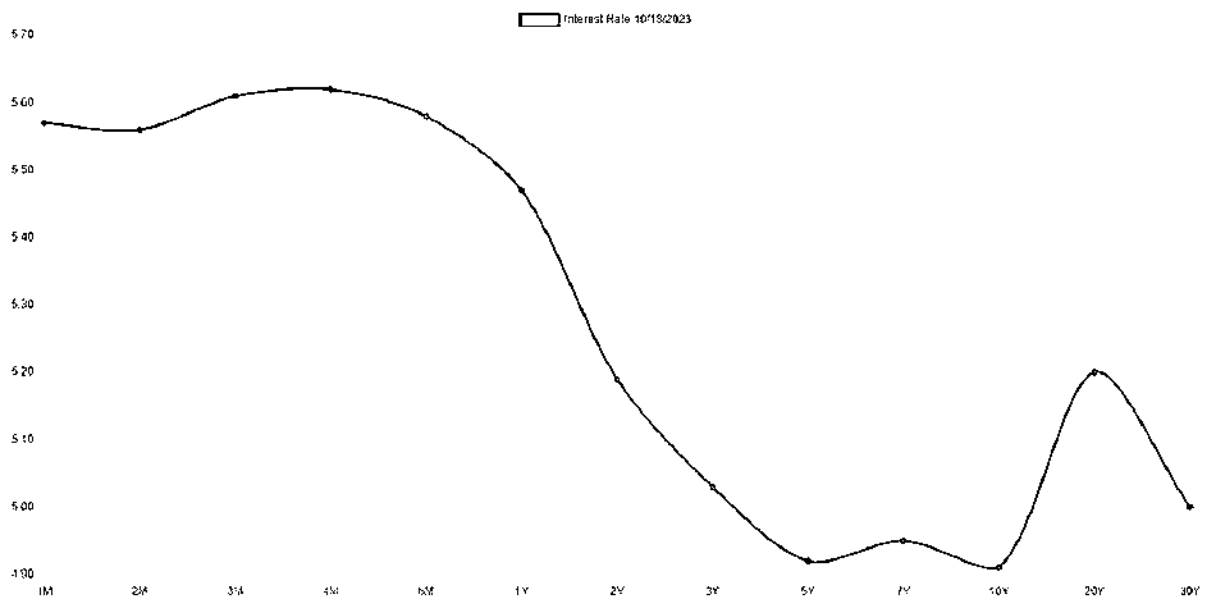
¹⁶ ERCOT Finance and Audit Committee Meeting, Item 5.2: Periodic Report on Investments at 5 (Oct. 16, 2023) (available at: <https://www.ercot.com/files/docs/2023/10/06/5.2%20Periodic%20Report%20on%20Investments.pdf>).

Figure 5: Chart Summarizing ERCOT's Money Market Portfolio¹⁷

Electric Reliability Council of Texas, Inc. Investment Compliance August 31, 2023 (\$ in 000's)				
Money Market Mutual Funds (MMMF)	Funds Held at ERCOT (Ending Balance)	Funds Held at Trustee (Ending Balance)	Month End Yield	Monthly Investment Income
ERCOT, Inc. Unrestricted	\$ 2,517,811	\$ -	N/A	\$ 8,519
ERCOT, Inc. Restricted (Collateral)	1,954,076	-	N/A	9,233
Total ERCOT, Inc. MMMF	\$ 4,471,887	\$ -	5.21%	\$ 17,751

Further, it is clear that the projected yield on treasury bonds is expected to remain well above 5% for at least the next two years. Below is a treasury yield curve that projects interest rates of around 5.2% two years from now:

Figure 6: Projected Treasury Yield Curve¹⁸



Given the statements that ERCOT has made in its own financial reports, as well as publicly available economic data, the interest income projections in ERCOT's Budget Submission do not

¹⁷ *Id.*

¹⁸ Pulled from <https://www.ustreasuryyieldcurve.com/> on October 20, 2023.

appear to be reasonable. Notably, ERCOT's recent Supplemental Budget Submission acknowledges that its projected interest income for 2023 is actually \$27.3 million higher than was expected at the time ERCOT prepared the original Budget Submission.¹⁹ However, as ERCOT stated in that supplement, the update "only revises ERCOT's 2023 favorable financial variance"²⁰ (i.e. the surplus calculated for 2023), but not assumptions going forward. In other words, ERCOT is not proposing *any adjustments* to reflect these recent, documented changes in interest rate expectations for 2024/2025 budgeting purposes. The Commission should require ERCOT to rework its budget submission to more accurately reflect the current interest rate environment.

3. There is no basis for ERCOT to assume that the CRR Fund balance will plateau at \$2.0 billion.

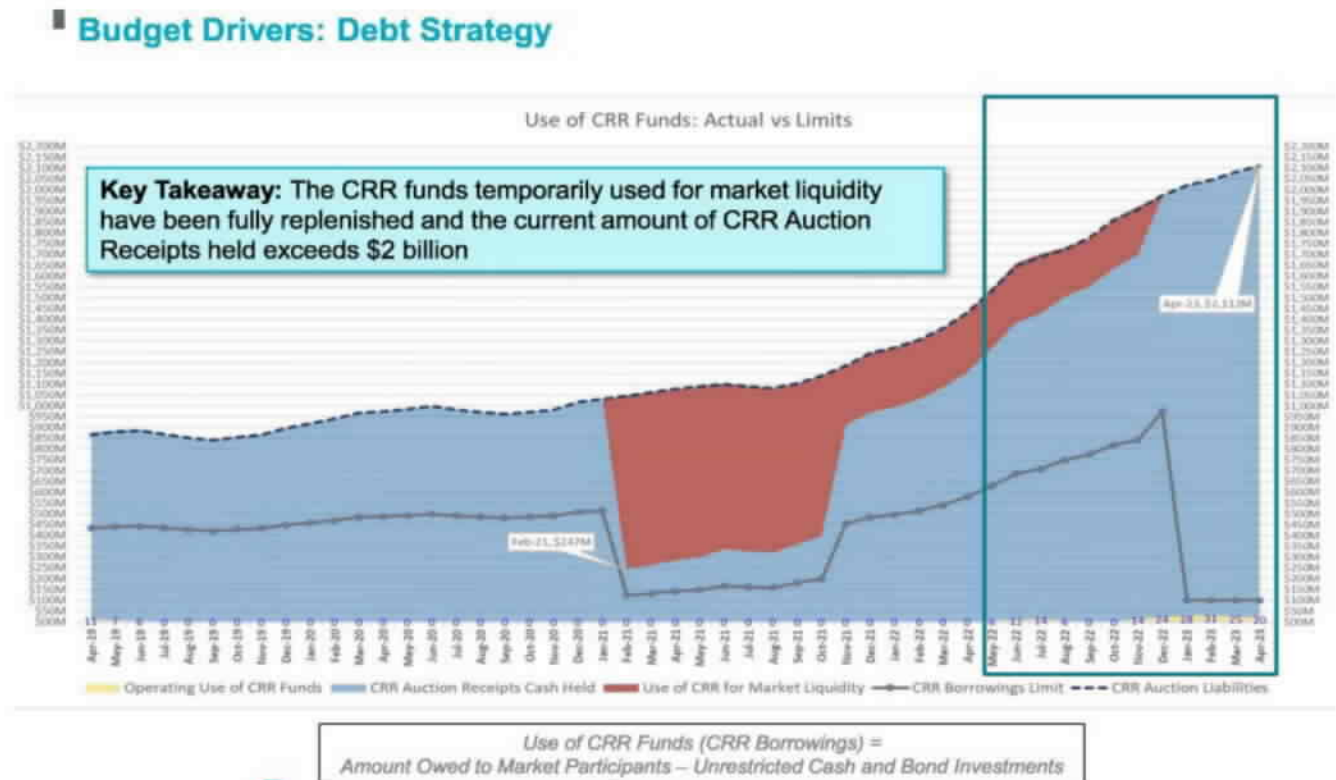
ERCOT also assumed the CRR Fund balance would fall from its current level of \$2.0216 billion to \$2.0 billion, and would stay at a constant \$2.0 billion between 2024 and 2029.²¹ ERCOT does not explain why it believes the CRR Fund balance will plateau, and that expectation is contrary to the consistent upward trend in the CRR Fund balance in recent years, as illustrated by the chart below:

¹⁹ Supplemental Budget Submission at 1.

²⁰ *Id.* (emphasis in original).

²¹ Budget Submission at 18, line 18; *id.* at 56.

Figure 7: Chart Showing Growth of CRR Fund Balance Over Time²²



The CRR Fund balance grew by **43%** over the last year and grew at a compound growth rate of over **25%** from 2019-2023. In light of this historical data, ERCOT's assumption that the CRR Fund balance will fall below its current level to \$2.0 billion and stay there for the next six years is not credible.²³ The Commission should also take a careful look at this assumption and alternative scenarios when evaluating ERCOT's Budget Submission.

4. Applying more reasonable assumptions for interest income could significantly reduce or even eliminate the required System Administration Fee increase.

As discussed above, ERCOT did not justify its expectation that the interest income it earns will drop precipitously in the next two years. That expectation drives nearly all of the requested increase in the System Administration Fee. To illustrate, assuming that the CRR Fund balance

²² *Id.* at 59.

²³ *Id.* at 18, Line 18; *id.* at 56.

averages \$2.5 billion over the next two years (which implies growth of less than 25%) and that ERCOT continues to earn the current expected yield of 5.21% on the funds held in its money market accounts, then its interest income would be approximately *\$130 million per year*,²⁴ or roughly \$80 million more than ERCOT's projected interest income for 2024.²⁵ Spread over 465 TWh (the expected usage in 2024), this additional interest income would reduce ERCOT's System Administration Fee request by \$0.172/MWh, from \$0.690/MWh²⁶ down to \$0.518/MWh—which is even lower than the *current* System Administration Fee. Even reducing the average CRR Fund balance to \$2.25 billion in that calculation would result in approximately \$72 million in additional interest income and a required System Administration Fee of only \$0.546/MWh—or nearly exactly the current fee. Given the dramatic impact that ERCOT's interest rate assumptions have on the required System Administration Fee, the Commission should not approve ERCOT's Budget Submission without further justification.

B. ERCOT should have further evaluated “Option 2,” which would require a substantially smaller up-front increase to the System Administration Fee.

As explained above, given the current interest rate environment, it does not appear that an increase in the System Administration Fee is even necessary. That said, if the Commission wants to consider a modest System Administration Fee increase, it should consider ERCOT's “Option 2” as a more reasonable alternative.²⁷ ERCOT's submission almost exclusively evaluates “Option 1,” which involves increasing the System Administration Fee to \$0.71/MWh in 2024 (ERCOT reduced this to \$0.69/MWh in its Supplemental Budget Submission²⁸) and keeping it there for the next four years.²⁹ However, ERCOT also describes “Option 2,” which would increase the System

²⁴ $\$2.5 \text{ B} * 0.0521 = \130.25 M .

²⁵ *Id.* at 18, Line 11.

²⁶ ERCOT's Supplemental Submission decreased its System Administration Fee request from \$0.71/MWh to \$0.69/MWh. Supplemental Budget Submission at 1.

²⁷ *See* Budget Submission at 61.

²⁸ Supplemental Budget Submission at 5.

²⁹ Budget Submission at 61.

Administration Fee to \$0.635/MWh³⁰ for 2024/2025, and then contemplates a subsequent fee increase for 2026/2027 if necessary. Given that financial projections become increasingly uncertain as the time frame is extended, and given current consumer cost concerns in ERCOT, TIEC recommends considering a more moderate System Administration Fee increase that can be reevaluated in ERCOT's next budget submission for 2026/2027. This more incremental approach will protect customers ratepayers against unnecessarily high System Administration Fee charges that will be locked in for several years.

C. ERCOT did not provide sufficient detail to justify its request for additional legal and public relations employees under “Strategic Objective 3.”

Third and finally, the Commission should require ERCOT to provide additional information to justify the increase in certain employee positions and department budgets surrounding ERCOT's legal and government/regulatory functions. ERCOT's “Strategic Objective #3” is to “Advance ERCOT, Inc. as an independent leading industry expert and an employer of choice by fostering innovation, investing in our people, and emphasizing the importance of our mission.”³¹ As part of that, ERCOT states that “Additional key incremental costs and employee positions include resources for improving communications and providing support for lawsuits, disputes, and regulatory requirements.”³²

Strategic Objective #3 includes adding eight new employees to ERCOT's General Counsel's office and increasing that department's budget by \$11.3 million per year, in addition to six incremental employees and \$4.1 million under Strategic Objective 1, for a total budget increase of \$15.4 million.³³ ERCOT has also budgeted to add two new Public Affairs positions and add \$1.9 million to that department's budget.³⁴ This is on top of using leasing office space near the Capitol to interface with legislators. It is difficult to tell from ERCOT's submission what exactly

³⁰ In ERCOT's original Budget Submission, this number was \$0.655. *Id.* The Supplemental Budget Submission reduced the proposed System Administration Fee by \$0.02/MWh, and the number above includes that adjustment.

³¹ *Id.* at 10.

³² *Id.* at 11.

³³ *Id.* at 34. Included among the Strategic Option 3 employees are 6 new positions to help ERCOT handle a “multitude of lawsuits and disputes, and substantial increase in complex regulations.” *Id.* at 39, line 9.

³⁴ *Id.* at 34.

these new employees will be doing, what portion of this increase is for the new salaries versus increased compensation for existing employees, and whether these new positions and increased budgets are appropriately charged to customers. Similarly, ERCOT does not provide any detail on the \$23.2 million in additional costs it has earmarked to “address recruiting and retention risks, including incentive programs and market adjustments,”³⁵ so it is difficult to evaluate whether ERCOT’s intended raises and incentive programs are reasonable. These are substantial amounts that, without further information, could be unreasonable and excessive for ERCOT customers to fund. Accordingly, TIEC suggests that the Commission request additional detail from ERCOT so it can fully vet these projected expenditures before approving them.

III. CONCLUSION

Based on the analysis above, TIEC does not believe any increase to the System Administration Fee is necessary. TIEC appreciates the opportunity to provide these more detailed written comments and looks forward to working with ERCOT and the Commission as this project moves forward.

³⁵ See Project No. 38533, ERCOT’s Summary Regarding Primary Variances from the 2023 Budget to the 2024 Budget Request and Impact on the System Administration Fee Rate of Certain 2024 Budget Request Components at line 8, bullet 2 (Oct. 12, 2023).

Respectfully submitted,

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